FARMERS' NEWSLETTER

Cotton

February 80/C-11

U.S. cotton producers have now provided the first hint of their plans for the 1980 crop. In a survey taken around January 1, they reported intentions to seed about 14 million acres--virtually the same as last year.

Of course, much can happen between now and planting time to alter these early plans. Changes in crop prices will be a determining factor. And weather developments might favor planting one crop over another.

This year, another factor is involved: the suspension of grain sales to the Soviet Union. This action was not announced until after farmers had their early planting intentions in the mail to USDA. It could lead to slightly larger cotton acreage in the spring.

In any event, you will probably be revising your acreage plans right up until seeding time. This letter is devoted to information that can be useful in making that decision.

Cotton Acreage Related to Price

Most important in determining how much land will be planted to cotton this spring is cotton's profitability compared with other crops, such as soybeans and sorghum.

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The next cotton newsletter is scheduled for early May.

This December, for example, producers in the Delta and Southeastern States saw cotton prices rising relative to soybeans. As a result, they indicated tentative plans to increase cotton acreage from 3.2 million last year to 3.4 million in 1980.

Meanwhile, cotton prices continued to rise against soybeans during January. If this trend persists for the next 2 to 3 months, farmers in these regions may decide to put even more land into cotton.

Likewise, while producers in the Southwest and West revealed plans in January to trim their cotton acreage slightly from last year's level, current price trends--if maintained--could lead them to change their minds by planting time.

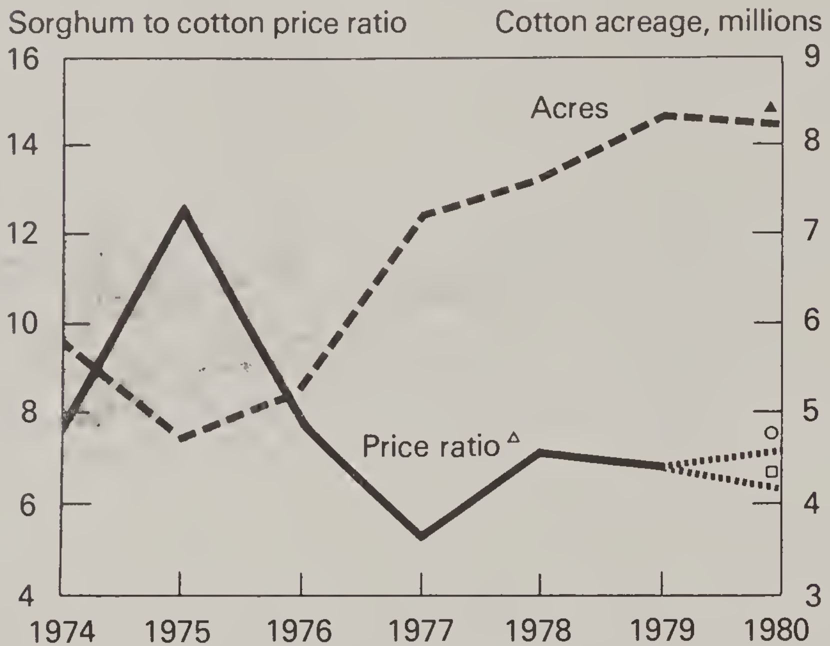
In short, the current outlook points to another large cotton harvest next fall. The odds are certainly against a repeat of last year's record yield of 551 pounds per harvested acre. But even assuming a normal yield and planted area of 14 million acres, 1980 fall production may exceed total use during the next marketing year. This, of course, would result in a buildup in U.S. cotton stocks and downward pressure on the price of your crop.

Chinese Demand Boosts Exports

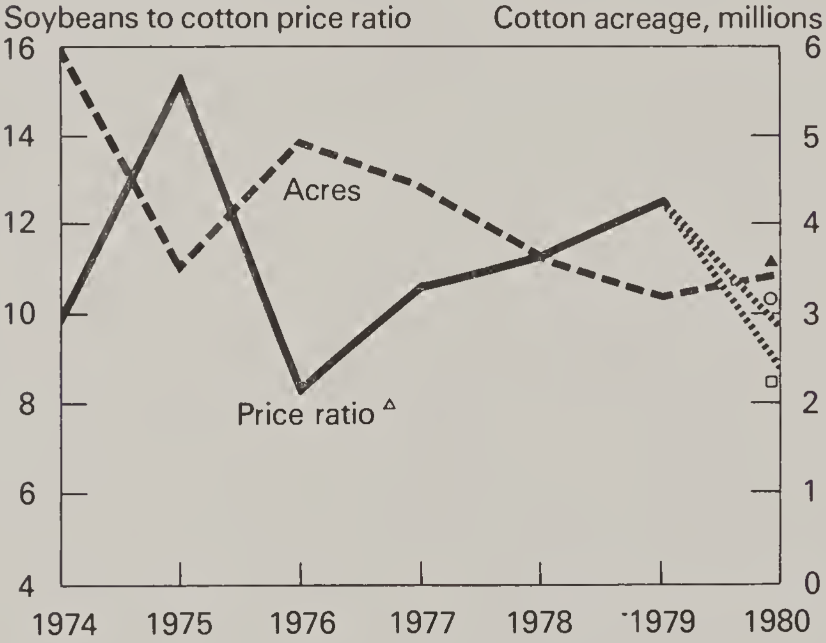
Currently, 8.6 million bales of U.S. cotton are committed for export this season. This includes shipments plus outstanding sales. Of this total, China accounts for 2-1/4 million bales,

HOW PRICES AFFECT COTTON ACREAGE

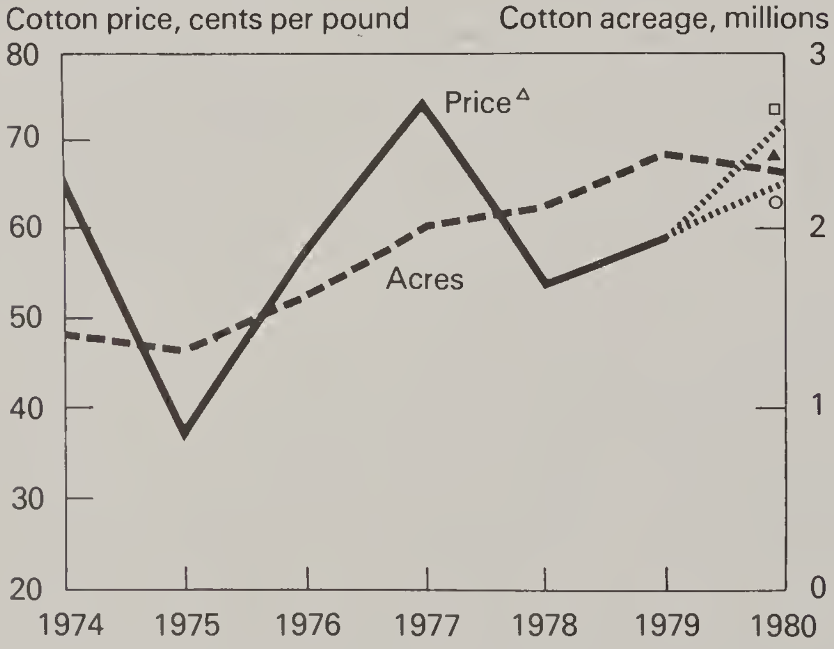
. . . In the Southwest



. . . In the Delta States and Southeast



. . . In the West



△ Average SLM 1-1/16-inch, February-March. ○ Average price in December 1979.
□ Average price in January, 1980 (first 3 weeks). ▲ January planting intentions.

substantially more than the 650,000 bales they bought from U.S. farmers last season. Thus, Chinese demand is the main cause of the sharp increase in cotton exports this season.

During the marketing season that begins next August, U.S. cotton exports will depend greatly on the gap between foreign cotton production and use.

The current high cotton prices could induce foreign producers to expand their cotton acreage in 1980, resulting in a crop larger than the 50.2 million bales produced in 1979.

This season, foreign mill use is estimated at a record-high 57.7 million bales--1.3 million more than last season. Consumption next season will be closely tied to world economic conditions, which may take a turn for the worse. If a world economic slowdown does occur, foreign demand for cotton could decline slightly.

To sum up, you can anticipate that the gap between foreign cotton production and use will narrow next season. Foreign cotton stocks next August could decline to 17.3 million bales--the lowest carryover since 1971. While this will maintain U.S. cotton exports at a high level compared with recent years, they are likely to fall short of this season's shipments by several hundred thousand bales.

Domestic Mill Use Holds Firm

Despite a sluggish economy, domestic mill consumption has held steady this season at about 6.4 million bales. Cotton prices have been more competitive with manmade staples, and the U.S. trade deficit in cotton textile products has improved--a combination that helped bolster domestic use. Depending on what happens to the economy, domestic use next season is likely to hold firm or perhaps increase slightly.

STOCKS ESTIMATED UP A FOURTH

	1978/79	1979/80	
		Projected	Range[1]
		Million 480-lb. bales	
Beginning stocks	5.3	4.0	
Production	10.9	14.9	±0.1
Total supply[2]	16.2	18.8	±0.1
Mill use	6.4	6.4	±0.2
Exports	6.2	7.5	±0.5
Disappearance[2]	12.5	13.9	±0.5
Ending stocks[2]	4.0	5.0	±0.5
		Cents per pound	
Farm price	58.4	[3]61.5	
Loan rate[4]	48.0	50.2	

[1] Chances are about 2 out of 3 that the outcome will fall within the indicated range. [2] May not add due to rounding. [3] Average: August-December, 1979. [4] For SLM 1-1/16" cotton.

Ending Stocks Estimate Lowered

U.S. cotton stocks next August 1 are now expected to total 5 million bales--one-fourth higher than last season's carryover, but down 300,000 bales from the previous estimate. Of this total, an unusually high proportion could be committed for export. Thus, "free stocks" are not quite as large as the total stock level would indicate.

Prices Showing Unexpected Strength

SLM 1-1/16-inch cotton is currently running about 16 cents a pound above year-earlier levels. This is much higher than the fundamental factors of supply and demand would suggest. For example, one primary indicator of price levels--the ratio between estimated total consumption and total supply--is the same this season as last, whereas spot prices are significantly higher.

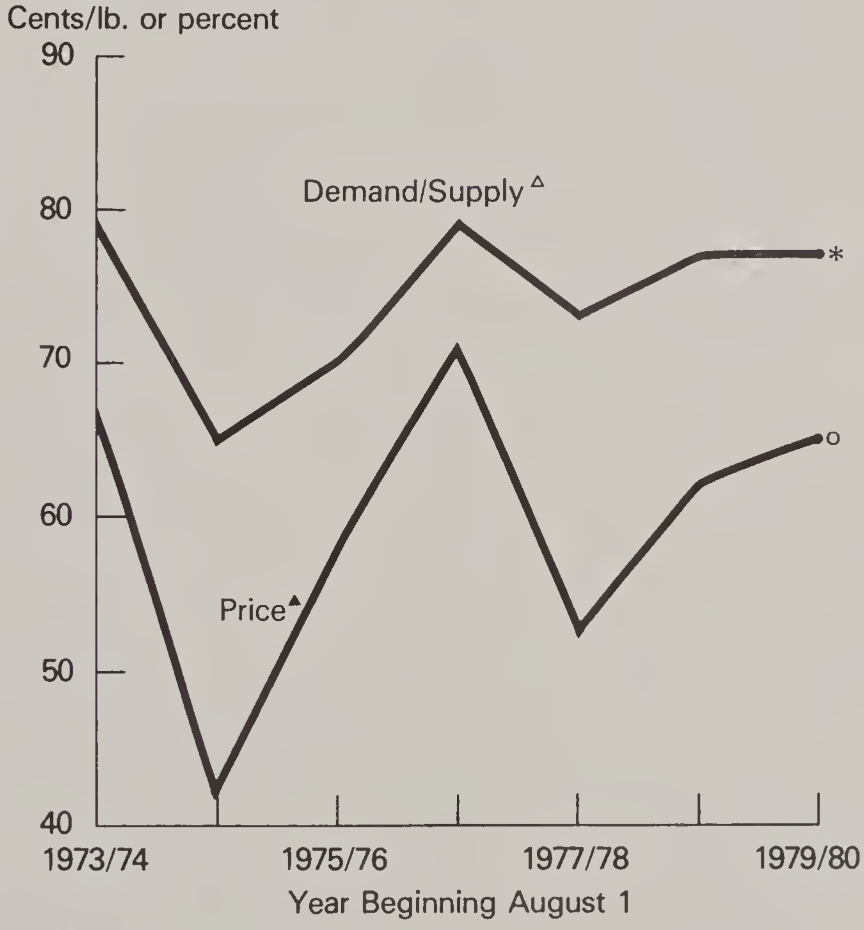
Then what accounts for the current price strength? Many have suggested it is due to a strong speculative element in the market, to international economic and political instability, and to a shortage of good-quality cotton.

Regardless, you are faced with a difficult problem: You must carefully assess whether cotton prices are likely to be higher or lower at harvest time than at planting time, and adjust your production plans accordingly. A prudent course of action would be to consider all opportunities for forward contracting.

Evaluate Your Planting Options

Farmers are often advised to use break-even price ratios as a "rule of thumb" in making planting decisions. For example, it is often stated that the break-even price ratio between soybeans and corn is 2.5 to 1; for soybeans and cotton, 10 to 1. These ratios suggest that if soybean prices are more than 2-1/2 times corn prices and more than 10 times cotton prices, soybeans would be more profitable than either corn or cotton.

COTTON DEMAND STILL STRENGTHENING



△ Mill use plus export sales divided by total supply.
▲ Average for SLM 1-1/16 inch cotton.
* Most likely outcome based on January conditions.
o Average through January, 1980.

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This concept is often very useful. However, as prices, costs, and yields change, so do break-even prices, and the ratio itself. The soybean/cotton break-even ratio of 10 to 1, then, applies only to a given set of prices, costs, and yields. It will vary from year to year and from farm to farm.

Using the following formula, you can compute more precisely the price you will need to receive for your cotton to make your profits equal to those from competing crops. As an example, say you are a soybean-cotton producer and expect the following prices, costs, and yields:

Item	Cotton	Soybeans
Price	?	$6.25/bu.
Costs per acre	$275	$85
Yields per acre	500 lbs.	23 bu.
Cottonseed value	$40/acre	0

Now, to compute the price of cotton that will produce profits comparable to those from soybeans under these conditions, use the following formulas:

1) Profits from soybeans:

($6.25 x 23) - $85 = $58.75/acre

2) Costs of producing cotton after subtracting the value of cottonseed:

$275 - $40 = $235/acre

3) Then the break-even cotton price will be:

$$\frac{(\$58.75 + \$235)}{500 \text{ lb./acre}} = \$.59/\text{lb.}$$

So in this example, you would have to get 59 cents a pound for your cotton to cover costs and to make your crop as profitable as growing soybeans. If you expect to sell your cotton for less than 59 cents a pound, soybeans would be more profitable, and vice versa. In this case, the break-even price ratio is 10.6 to 1 (or $6.25 to $0.59).

Now, suppose you expect soybeans to yield only 20 bushels per acre, with nothing else changed. Then your net returns from soybeans would be:

($6.25 x 20) - $85 = $40/acre

And your break-even cotton price would be:

$$\frac{(\$40 + \$235)}{500 \text{ lb./acre}} = \$.55/\text{lb.}$$

In this case, the break-even price ratio is 11.4 to 1 (or $6.25 to $.55).